

## Exhibit D

### Low-Mod Fund Excess Surplus

Excess Surplus is defined and calculated based on provisions in Health & Safety Code Section 33334.12. Excess Surplus is determined on the first day of each fiscal year. The calculation requires comparing the sum of tax increment deposited over the previous four fiscal years against the agency's adjusted beginning balance (prior year's ending adjusted unencumbered balance) to determine which amount is greater. Agencies are allowed to adjust their unencumbered balance to exclude the amount of unspent proceeds from the sale of bonds and the difference between the prices of land sold during the reporting period compared to the land's fair market value. By statutory definition, Excess Surplus exists when the adjusted unencumbered balance exceeds the greater of: (1) \$1 million or (2) the combined amount of tax increment revenue deposited over the preceding four fiscal years.

Fifty-one agencies reported having Excess Surplus totaling \$115 million, in FY 2003/04, more than double the \$53 million reported in the previous fiscal year. When Excess Surplus is identified, the law requires agencies to either: (1) transfer Excess Surplus to the local county housing authority within one year or (2) spend or encumber all the remaining Excess Surplus within two additional years from the time limit given to transfer funds to the county housing authority. Health & Safety Code Section 33334.12(e) specifies severe penalties for not eliminating Excess Surplus within three years, which include: (1) limiting an agency's actions such as preventing the agency from encumbering and spending its funds and (2) charging the agency's other (non-housing) funds an amount equal to 50 percent of the amount of Excess Surplus that must be deposited to the Low-Mod Fund. To date, no agencies have reported Excess Surplus beyond the three year time period to incur penalties.

Excess Surplus and provisions relating to penalties were enacted into law (Chapter 942, Statutes of 1993, AB 1290) with some provisions amended in 1999 and 2001. To remedy problems in correctly determining and reporting Excess Surplus, Chapter 442, Statutes of 1999 (AB 634), requires the agency's independent auditor to calculate Excess Surplus based on audit guidelines prescribed by the State Controller's Office in consultation with the Department and to report the existence of Excess Surplus in the agency's annual audit. In addition, the State Controller and the Department must be provided a copy of the agency's independent annual audit. In 2001, a new provision was added (Chapter 741, Statutes of 2001, SB 211) specifying that before an agency can amend its redevelopment project area plan to extend certain time limits to incur debt and continue to receive tax increment, the agency must first submit data to enable the Department to confirm the agency has not accumulated Excess Surplus.